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COMMONWEALTH OF VIRGINIA

STATE CORPORATION COMMISSION

AT RICHMOND, January 28, 1999

APPLICATION OF

CASE NO. PUA980037

VIRGINIA ELECTRIC AND POWER COMPANY

For approval of affiliate transactions with  
Virginia Power Services Energy Corp., Inc.

**ORDER GRANTING APPROVAL**

On October 30, 1998, Virginia Electric and Power Company (“Virginia Power,” “the Company,” “the Applicant”) filed an application with the Commission under the Public Utilities Affiliates Act requesting approval of affiliate transactions with Virginia Power Services Energy Corp., Inc. (“VPSE”). As stated in the application, VPSE is a general business corporation organized under the laws of the Commonwealth of Virginia. Virginia Power Services, Inc. (“VPS”) is the sole shareholder of VPSE. As indicated in application, VPSE’s primary business will be to manage fuel-related activities of Virginia Power. These fuel-related activities include the purchase, sale, storage, and transportation of natural gas, gasoline, oil, and diesel fuel (collectively referred to as “Fuel”) for Virginia Power’s benefit and to provide Virginia Power with associated risk management services (“VPSE Services”). As indicated in the application, VPSE will provide the VPSE Services to Virginia Power pursuant to an Agreement.

In the application, Virginia Power requests approval to enter into an Agreement with VPSE for the provision of VPSE Services to Virginia Power. As indicated by Virginia Power,

Virginia Power Energy Marketing, Inc. (“VPEM”) will serve as VPSE’s agent for performance of the VPSE Services pursuant to the Fuel Agency and Service Agreement between Virginia Power Services Energy Corp., Inc., and Virginia Power Energy Marketing, Inc. (“Agency Service Agreement”). The Agreement provides that Virginia Power will transfer to VPSE contracts to store natural gas in states other than Virginia and contracts to transport Fuel to facilities owned or operated by Virginia Power or to which Virginia Power is obligated to provide Fuel. Virginia Power provided a list of contracts to be transferred with its application. Virginia Power also will transfer natural gas and oil owned by Virginia Power (“the Energy Assets”) to VPSE. A list of such assets as of September 30, 1998, also was provided with the application. VPSE also will deliver Fuel to Virginia Power upon request. Title shall transfer from VPSE to Virginia Power upon delivery. As part of the Agreement, Virginia Power will make available to VPSE oil storage facilities and will operate and maintain those facilities to accommodate the provision of the VPSE Services. The Agreement may be terminated with ninety days’ written notice.

As stated by Virginia Power, the Company will continue to enter into fuel related arrangements following the filing of the application. Therefore, the Agreement provides that Virginia Power will transfer to VPSE contracts in addition to the contracts listed in the attachment filed with the application. Virginia Power will transfer to VPSE various contracts entered into by Virginia Power during the time period between the filing of this application and a reasonable time after approval by the Commission. Similarly, the Energy Assets to be transferred by Virginia Power to VPSE will vary from the list provided as a result of Virginia Power’s acquisition and use of natural gas and oil after September 30, 1998.

The Agreement also provides that, upon request of VPSE, Virginia Power may guarantee the full and prompt payment of any amounts payable to a third party from VPSE arising out of a contract entered into between the third party and VPSE or arising out of any contract assigned to VPSE by Virginia Power.

Under the Agreement, VPSE will provide the VPSE Services, through its agent VPSE, for Virginia Power. Virginia Power will pay VPSE an amount equal to the actual costs VPSE incurs on behalf of Virginia Power including commodity costs, service charges, storage and transportation costs, and any other costs. The transfer of contracts will be at no cost, and the transfer of the Energy Assets will be at book value.

As represented by Virginia Power, the reason for the proposed arrangement is for tax purposes. As indicated in the application, a major portion of the Company's natural gas inventory is stored in locations outside of Virginia. The transfer of out-of-state storage, and the transportation rights associated with transporting such natural gas in storage from Virginia Power to VPSE is part of Virginia Power's effort to segregate the Company's out-of-state activities from its state activities. The Company represents that by transferring out-of-state activities from Virginia Power to VPSE, Virginia Power will avoid having its taxable income subject to state income taxes as a result of those out-of-state activities. To the extent such activities create nexus in states other than Virginia, North Carolina, and West Virginia, VPSE will be subject to state income taxes at a much lesser amount because Virginia Power's taxable income will not be used to compute the state tax amount. The Company states the requested approval is in the public interest because the provision of the VPSE Services through a separate subsidiary will permit Virginia Power to avoid establishing nexus and income tax liability in states other than Virginia,

West Virginia, and North Carolina. The Company further represents that no additional or unnecessary costs will be imposed on Virginia Power's electric customers.

THE COMMISSION, upon consideration of the application and representations of the Applicant and having been advised by its Staff, is of the opinion and finds that the above-described Agreement with Virginia Power Services Energy Corp., Inc., is in the public interest and should be approved subject to certain limitations as to Virginia Power's guarantee of obligations. Accordingly,

IT IS ORDERED THAT:

- 1) Pursuant to §56-77 of the Code of Virginia, Virginia Electric and Power Company is hereby granted approval of the Agreement with Virginia Power Services Energy Corp., Inc., under the terms and conditions and for the purposes as described herein.
- 2) The authority to guarantee the full and prompt payment to third parties shall be limited to obligations incurred on behalf of Virginia Power and shall not apply to obligations incurred for VPSE, VPEM or VPS to make off-system sales.
- 3) The Applicant shall file monthly financial statements of Virginia Power Services Energy Corp., Inc., with the Commission's Director of Public Utility Accounting.
- 4) Should any terms and conditions of the Agreement change from those contained in the Agreement approved herein, Commission approval shall be required for such changes.
- 5) The approval granted herein shall have no ratemaking implications.
- 6) The approval granted herein shall not preclude the Commission from exercising the provisions of §§56-78 and 56-80 of the Code of Virginia hereafter.

- 7) The Commission reserves the right, pursuant to §56-79 of the Code of Virginia, to examine the books and records of any affiliate in connection with the approval granted herein whether or not such affiliate is regulated by the Commission.
- 8) The Applicant shall bear the burden, during any future rate proceeding or earnings test filing as agreed to per stipulation in Case No. PUE980296, to show that, in connection with the contracts transferred to VPSE as approved herein, any releases of capacity and off-system sales to the market or any contracts transferred to third parties resulted in reduced costs to Virginia Power. Virginia Power must be able to identify such cost reductions and show how they were determined.
- 9) The Applicant shall file with the Commission a final list of contracts and Energy Assets transferred to VPSE pursuant to the approval granted herein within thirty days of completion of such list.
- 10) The Agreement approved herein shall be included in the Applicant's Annual Report of Affiliate Transactions filed with the Commission's Director of Public Utility Accounting.
- 11) This matter shall be continued generally subject to the continued review, audit, and appropriate directive of the Commission.